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UNITED DRUG COMPANY

EXECUTIVE OFFICES, BOSTON, U. S. A.

43 LEON STREET

BOSTON, MASS.

February 14, 1927.

To the Stockholders of
United Drug Company:

Your Company has completed another record year. The enclosed income statement and balance sheet tell of the progress and results for the year ending December 31, 1926. I find much satisfaction in reviewing this report, which reveals substantial improvement in sales and profits, and in addition, I am sure that the splendid work done by the entire organization during the year of 1926 will be reflected in the future development and progress of our business.

On behalf of the Directors, I extend my appreciation to the members of our Manufacturing and Retail organizations, who have so loyally supported the Management and so thoughtfully worked out the extensive expansion policy that we carried out last year.

The total sales of our consolidated companies in the United States alone amounted to $91,183,162.01, which represents an increase over the previous year's figures of over thirteen millions of dollars, or 16%. This establishes a new high record of sales.

Net income amounted to $8,883,146.74, which represents an increase over the previous year - net profit figures - of $873,000., or approximately 11%.

It will be seen that the increase in profit figures did not quite measure up proportionately to the increase in sales. However, I regard this showing as most satisfactory in view of the fact that approximately one-half of our total sales increase came from new retail stores, acquired or created in the year 1926.

The Liggett Company, our retail subsidiary, opened during the year of 1926, 123 new stores and closed 13 - or a net increase of 110. To give you a more vivid statement of that expansion, for the 14 months commencing November 1st, 1925 and ending December 31st, 1926, we opened 141 stores. This large expansion, which is unprecedented in the history of our Company, was accompanied by the usual preliminary and abnormal expenses incident to such an undertaking. Many of these new stores were opened during the latter part of the year, and should exercise a marked influence upon future operations, as every Liggett store is not only expected to make money, but is a direct and important outlet for the sale of our manufactured products.

After setting aside reserves for Federal Taxes, earnings on the Common stock amounted to $13.01 per share. This compares with $12.27 in 1925, $11.03 in 1924; $6.97 in 1923.

The foregoing figures of net income and earnings on our Common stock represent the income actually received by the Company, and is without taking

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into consideration our part of the undistributed earnings on our investment in Great Britain and Canada, which, notwithstanding last years disturbed conditions of Great Britain, will show a substantial amount.

The items appearing in the balance sheet are generally self explanatory, and have been chiefly affected by the expansion of the Liggett Company heretofore referred to. Our cash is down due to the retirement of approximately two millions of dollars of 8% Gold Notes heretofore outstanding, which matured on June 15th and were paid in full at that time. The balance of reduction in cash has gone into the purchase and equipping of new retail stores.

The substantial increase in Real Estate and Buildings as well as improvements to leaseholds is due to the purchases of prominent retail locations where we have been expanding.

The increase in Machinery, Furniture and Fixtures of approximately two and one-half millions of dollars has been almost all invested in fixture accounts for retail stores.

One item in the Balance Sheet to which I wish to call particular attention is the increase during the year in the amount of Common Stock outstanding, such increase amounting to $3,314,500. Approximately one million dollars of this amount represents the stock received at the time of liquidation of Liggett's International Ltd. sold to the Officers and Employees at par under the vote authorizing such action taken by the Stockholders at the Special Meeting held in January 1925. A corresponding amount from the same source will be sold each year during the life of the options outstanding, which expire January 1st, 1930. I believe that this action, which has enabled the Executive Officers and Managerial Heads of our parent Company and subsidiary companies to secure a substantial stock interest in the Company, has already been of decided benefit to the Company and its Stockholders, and will be of increasing benefit as the options mature and are taken up.

The balance of the increase in common stock outstanding represents the remainder of the stock taken by the bankers and completes the contract and option given them by the Board of Directors in 1924. At that time, we were contemplating the redemption of our 8% Bonds; we desired to simplify our financial structure; to call our Second Preferred Stock, and to eliminate outstanding obligations of our subsidiary companies, including the liquidation of Liggett's International Ltd., and the exchange of the 8% Preferred stock of that Company for the 7% Preferred stock of the United Drug Company. At that time, both the Preferred and Common stocks of the United Drug Company were selling below par, and, in order to accomplish our object, it was necessary to engage in a broad educational campaign to secure the interest of the investing public in our securities. Our bankers agreed to do this, and to sponsor our securities, and, in consideration, we gave them an option on 50,000 shares of stock at ten points above the then market. The result of their efforts, combined with the excellent showing of our companies, has enabled us to carry out and complete the program then embarked upon, and I feel that the Company has greatly benefited from the arrangement made.

A gratifying indication of the strength and resources of our business, is shown by the fact that we again wound up the year without bank borrowing, after having achieved the greatest expansion in our history, at an investment on the part of the Company of nine and one-quarter million dollars, and without resort to any financing other than that mentioned in the preceding paragraphs, nor do we know of anything that will call for any additional financing during the next year.

Our goal is to exceed $100,000,000 in the year 1927; and to show a corresponding increase in Net Profits. Our stockholders who are in the drug business are giving us splendid cooperation and are effectively distributing the products of our factories in their communities. Our stockholders who are not druggists can also play an important part in achieving this result through their patronage and influence on behalf of the Rexall and Liggett Stores.

Sincerely yours,

Louis K. Liggett

President